

**STATEMENT OF
SUSAN GAFFNEY, INSPECTOR GENERAL**

**BEFORE THE
COMMITTEE ON GOVERNMENTAL AFFAIRS
UNITED STATES SENATE**

**ON
HIGH RISK PROBLEMS AT HUD
MARCH 5, 1997**

Mr. Chairman and Members of the Committee, thank you for the opportunity to present the views of the Office of Inspector General (OIG) on programmatic and management problems facing the Department of Housing and Urban Development (HUD).

In our semiannual Reports to the Congress, the OIG attempts to provide an overview of HUD's management and performance during the reporting period. In our latest Report to the Congress, as of September 30, 1996, we summed up the situation in the following manner:

"The last few years have seen notable improvements in some aspects of HUD's performance. HUD and the Congress have, for example, moved to change the landscape of failed public housing and to address serious issues relating to the multifamily insured and assisted housing programs.

"Under current circumstances, however, the prospects for further improvement are dim. HUD's capability to perform is limited by three fundamental issues that have gone unaddressed and can be expected to become more serious over the years. Specifically:

- The number and varied types of HUD programs/initiatives are significantly out of balance with the capability of the constantly dwindling HUD staff to carry out those programs and initiatives.
- Various components of HUD, especially the Office of Public and Indian Housing and the Office of Multifamily Housing, are not equipped to provide reasonable stewardship over taxpayer funds expended for their programs.
- HUD's avowed commitment to a 'place-based' program

delivery approach is, in important respects, inconsistent with HUD's organization and authorities, which follow discrete HUD program lines.

"We do not believe that these issues can be resolved through easy or quick fixes. Bringing HUD programs in line with HUD staff capability would undoubtedly require a narrower, more precise definition of HUD's mission; and this would in turn provoke outcries from the many constituencies--both within and outside the Department--that have formed around HUD programs.

"Ensuring stewardship and accountability in HUD programs, especially the public and assisted housing programs, needs to start with an acknowledgement that HUD doesn't have and won't have the capability to carefully monitor all aspects of these huge programs. This would have to be followed by an assessment of the risks inherent in various approaches to setting program priorities, and development of systems that accurately measure program performance rather than just regulatory compliance.

"Resolving the inconsistencies between HUD's avowed commitment to a place-based orientation and the realities of HUD's program-based organization would again require a clearer definition of HUD's mission, potentially followed by a major shifting of authorities within the Department.

"In sum, resolution of these three issues would constitute a substantial agenda for both HUD and the Congress. We urge adoption of this agenda, on the grounds that it is fundamental to making HUD the excellent performer that we all want the Department to be."

Secretary Cuomo heard the same type of message during his recent confirmation hearings, and he has committed to acting on it. This past weekend, the Secretary and his Principal Staff held an unprecedented meeting at which they established an integrated management/program/organizational plan of action to address HUD's greatest vulnerabilities. So, there is reason to be optimistic about HUD's resolve to shed its high risk designation. But HUD alone cannot solve these problems. Significant changes in HUD's authorizing legislation are also essential.

To illustrate the magnitude of the task confronting the Department and the Congress, I would like to focus on two issues. First, the most significant programmatic issue facing the

Department: what the future will bring for assisted housing programs. Second, the most significant management issue facing the Department: the management of its staff resources.

ASSISTED HOUSING PROGRAMS

Issues relating to the funding, accounting, and monitoring of assisted housing payments represent the largest problem the Department faces. HUD currently spends more than \$18 billion per year to provide rent subsidies to about 4.5 million lower-income households. The assistance HUD provides is the most fundamental program for ameliorating the nation's growing need of housing for low income persons. The primary sources of this housing assistance are project based Section 8 payments to multifamily owners, tenant based Section 8, and other subsidy payments to Housing Authorities.

Budget Issues

As you are well aware, renewals of project based section 8 contracts have major budget implications as Congress attempts to balance the Federal budget. If these contracts are not renewed, currently assisted tenants will face sharp increases in their rental payments. For many assisted low income tenants, the slightest such increase could result in their displacement. From the owners' perspective, failure to renew project based Section 8 contracts for heavily assisted projects could sharply reduce project revenues and result in an increase of defaults and insurance claims.

In the late 1970s and early 1980s, it was common for section 8 assistance payments contracts to be written for multiple years. Funds were obligated during the initial contract year with a federal commitment to fund outlays in future years. These long term contracts had a negligible outlay impact in the year in which the appropriation was made. Through this budget mechanism, substantial increases have been made in program levels, evading normal budgetary controls that tended to focus on limiting outlays. The Department has an array of outstanding 20, 15, 10, and 5 year Section 8 contracts.

Because of Congressional efforts to lower Federal budget outlays, new or renewed section 8 contracts are now being made for only one year. The cascading effect of the expiring long

term contracts being renewed for one year will have significant budget implications for HUD in future years. For example, in five years, the annual budget authority needed to renew expiring section 8 contracts will be \$20.5 billion dollars. This is an increase of nearly \$15 billion dollars over 1997 budget authority.

Compounding this problem is the fact that a significant portion of HUD's insured subsidized multifamily housing projects has rents in excess of comparable market rents. Many of HUD's insured projects were developed to increase the stock of affordable housing at a time when few private developments were being constructed. High interest rates and high construction costs resulted in over financed multifamily housing projects. Market realities did not enter into many of the decisions to develop these HUD projects. Also, annual rent increases were approved based on formulas or budget computations with little comparison to the private market. Consequently, rents associated with these HUD subsidized projects are often much higher than rents at comparable projects.

Last year, HUD proposed legislation to address the contract renewal and excessive rents problems through portfolio reengineering. The proposal met with considerable resistance, and the Congress authorized only a small portfolio reengineering demonstration program. HUD is now working on a revised proposal to meet the same goal: reducing mortgage debt to a level that can be supported by comparable street rents. The restructuring of the debt would allow owners to continue operating the projects and significantly reduce the associated cost of the HUD section 8 subsidy. This restructuring effort would initially be costly, but is intended to be cost effective in the long run. The tax implications of such restructuring for owners remains a complex and contentious issue.

Accounting and Financial Management System Issues

The Department does not have efficient, effective, and integrated financial management systems that can be relied upon to provide timely, accurate, and relevant financial information and reports. While we have seen some progress in the development and implementation of needed systems, the pace has been slow.

To HUD's credit, progress has been made in getting the systems for budgeting and accounting for project based rental assistance programs (TRACS) and the similar system for tenant based assistance (HUDCAPS) up and running. However, certain critical components of these systems that would help to validate

the accuracy of assistance payments are still under development.

HUD's system plans only recently began addressing verification of tenant reported income under HUD's multifamily rental assistance programs. For Public and Indian Housing Programs, plans have been developed to use computer matching techniques to verify tenant reported income on a pilot basis. However, in the Department's effort to complete nationwide matching, errors and missing data were found in the Multifamily Tenant Characteristic System (MTCS). MTCS is critical to this matching effort.

The Department is making a concerted effort to develop TRACS as the solution to address weaknesses in the financial control of project-based rental assistance. Critical to this development is the payment processing module, which has not been built. This module would enable TRACS to generate rental assistance payments requests directly without voucher data from the owners. This would prevent duplicate payments and ensure the accurate submission of tenant data from the owner.

Monitoring Issues

HUD's monitoring of assistance payments is largely ineffective. HUD legislation authorizing subsidy programs includes specific tenant eligibility criteria. Legislation also establishes minimum performance levels to be achieved such as subsidized housing meeting housing quality standards. HUD is not currently equipped to ensure that these legislative mandates are being met.

One of HUD's major goals is to assure that limited Federal assisted housing resources are used as efficiently as possible. A recently issued quality control review, contracted for by HUD's Office of Policy Development and Research, looked into the accuracy of subsidy payments in a nationwide sample. The review found significant subsidy payment errors, including over and under payments. When projected to the population of subsidized tenants, the study found annual overpayments of \$788 million and underpayments of \$603 million.

In reviewing the accuracy of tenant based assistance, HUD generally relies on the annual audits of Public Housing Authorities (PHAs) by Independent Auditor (IAs). The IAs are required to test for tenant eligibility and test the validity of the operating subsidies. OIG reviews of these annual IA audits have found their primary focus to be on internal controls with little substantive testing. HUD staff may also test tenant

subsidy and operating subsidy computations during site reviews; but, due to staffing limitations, such reviews are becoming less and less frequent. We are working with HUD staff to explore ways to increase the testing performed by IAs, and thereby improve the usefulness of the IA reports.

With respect to Section 8 project based assistance, owners draw their monthly subsidy payments through a letter of credit disbursement system. These disbursements are subject to a post review process. HUD field offices are required to review a minimum of 20 percent of the Section 8 disbursements and determine that they are supported by vouchers. They are also required to compare a sampling of vouchers against the TRACS database to assure that tenant information is being updated as required.

In 1996, HUD established a voucher processing Hub in Kansas City. Currently, the Hub has taken over the voucher review process for 17 field offices and is scheduled to take it over all offices by next year. We examined the testing performed by the Hub and the testing at 5 other field offices. We found, with the exception of one field office, that the Hub was the only place where voucher reviews were being conducted. The good news is that the Hub is doing its job. The bad news is that before establishment of the Hub, this post review effort was largely not happening. Without post reviews, there is no assurance that payments are correct.

Our fiscal year 1994 financial report noted that HUD planned to use TRACS in the future for payment processing. HUD planned to implement an interface with the payment system in 1996. Because of funding problems, this interface is not scheduled for completion until Fiscal Year 1998.

RESOURCE MANAGEMENT

Since 1980, HUD staffing has dropped by 37%--from 16,500 to 10,434--and HUD has committed to a staffing level of only 7,500 by fiscal year 2000. The number of programs and initiatives these employees are responsible for managing is overwhelming. Two years ago, the Secretary asked for the OIG's views on opportunities for terminating, consolidating, and restructuring HUD programs. We conducted a study that, among other things, identified 240 discrete HUD programs and activities. In response to a Congressional request, the OIG is in the process of compiling a current list of discrete HUD programs and activities. I do not expect to find a reduction in the number of programs and activities over the last 2 years. But there are certainly fewer

HUD staff than 2 years ago. Subtracting programs seems to be a lot tougher than adding them.

Both HUD and Members of the Congress have proposed legislation to streamline HUD programs, but, with one exception, these legislative proposals have not been enacted. Meanwhile, HUD has proceeded to formulate downsizing plans without regard to their programmatic implications. Generally, staffing reductions have been allocated among the Assistant Secretaries on a pro rata basis. HUD also reorganized itself along program lines, with authority flowing directly from the Assistant Secretaries at Headquarters to the program staff at HUD field offices. Shortly after reorganizing in that manner, HUD proclaimed its commitment to a community-first, place-based (vs. program-based) delivery system.

The OIG believes that HUD's downsizing creates a series of urgent needs that the Department and the Congress must meet. We need, first of all, to come to a definition of HUD's mission that bears some reasonable relationship to HUD's capability to meet that mission. The revised mission statement must then be used as a springboard for a major streamlining of HUD programs and activities.

We must also come to an understanding that HUD staff cannot be all things to all people. We owe HUD employees a clear definition of their roles with respect to policy development, providing technical assistance, motivating the community, overseeing program implementation, and taking enforcement action for inadequate performance.

Even with a narrower mission statement, streamlined programs, and a clear understanding of the role of HUD staff, the OIG does not think that the downsized HUD will be able to provide traditional oversight of HUD programs. We believe, instead, that there will still be a compelling need to segregate HUD's workload based on risk, define different HUD oversight strategies for the different risks, establish meaningful performance measures, and develop a real enforcement capability.

Permit me to emphasize the importance of meaningful performance measures and a real enforcement capability. As you know, the point of the Government Performance and Results Act (GPRA) was to ensure meaningful performance plans and performance measures. We must diligently guard against making compliance with this law into a bureaucratic exercise. I have, for instance, heard GPRA advocates cite HUD's Public Housing Management Assessment System (PHMAP) as a model. In fact, PHMAP is the antithesis of what we should be looking for, because it

measures management processes and ignores whether we are achieving the desired program outcome, which is decent, safe, and sanitary public housing. As a result, we have situations where public housing authorities are not deemed troubled based on their PHMAP scores, but the residents are in fact living in squalor.

The HUD OIG has complained for years about the Department's reluctance to take enforcement actions against persons and entities that misuse our funds and abuse our programs. In this era of devolution, the issue has become critically important--not just for HUD, but for all Federal agencies. We cannot assume that the States, localities, non-profits, and other recipients of Federal funding will always act with wisdom and integrity. We should be dedicated to establishing meaningful performance measures and oversight, coupled with the resolve to move decisively against cases of fraud or abuse. In this regard, the HUD OIG has proposed a series of legislative measures that we believe would significantly strengthen HUD's enforcement capability. Mr. Chairman, I have sent copies of these proposals to you, as well as to the other Committees having oversight responsibilities for HUD.

In closing, I would like to remind you that I am heartened by Secretary Cuomo's understanding of HUD's areas of high risk, and his determination to fix them. I would also like to note two important pieces of legislation that the OIG believes are moves

in the right direction. HR 2 would bring about a major consolidation of public housing funding, among other things. HR 217 would consolidate Federal programs for homeless assistance.

Mr. Chairman, I would be happy to answer any questions you may have.

HUD is undertaking major organizational changes. Moreover, HUD has targeted its staffing level to be at 7500 by the year 2000. These staff decreases have been made without a corresponding reduction in workload. In fact, not only has the workload in many of the existing programs grown but several new programs have been added. HUD's staffing changes have been on a different track than HUD's programmatic and organizational changes. Consequently, there is a lack of resources given the current structure of the Department.

HUD's reinvention efforts began late in 1994, when the Secretary proposed significant changes in HUD's programs and operations. Sixty of HUD's grant and subsidy programs would be consolidated into three performance funds. Public Housing tenants would be given vouchers and Public Housing Authorities would need to be good performer in order to keep their housing voucher holders. FHA would be transferred to a new government owned Federal Housing Corporation. This corporation would adapt easily to management demands and customer needs. The corresponding staff downsizing made better sense in terms of what HUD planned for in reinvention.

In January 1996, HUD updated the reinvention plans. The new HUD blueprint would not voucher out public housing as originally proposed. The focus of Public Housing improvements would be in tenant based program delivery. Changes in Community Planning and Development would consolidate twenty various grant programs into three performance based funds including, Community Development Block Grants, HOME funds and Homeless assistance funds. The proposal for a separate Federal Housing Corporation was eliminated in favor of performance improvements within the existing FHA.

Other changes in the blueprint include:

- implementing the proposed communities-first, placed based program delivery structure;
- redeploying 500 headquarters and 1,000 field staff;
- closing 10 of the 81 HUD field offices;
- moving towards service center operations; and
- implementing a paperless office concept on a pilot basis.

Some progress has been made in recent months in bringing many of these blueprint concepts into fruition. HUD has made partial reductions in headquarters staffing and redeployed 600

field staff to help in correcting staffing imbalances. Seventeen field offices have been conceptually identified for closure. Several operations such as Single Family Housing, Accounting and Administration have been consolidated into field service centers. These centers handle consolidated functions for a number of field locations. While some changes have been made, HUD had not clearly established the role, level and distribution of resources needed to carry out proposed changes to HUD's program delivery structure.

Efforts to correct staffing and management deficiencies in the Department have largely been done in isolation. Top management discuss broad organizational concepts such as "Creating Communities of Opportunities" or developing a "Placed Based" HUD where communities have a single point of contact, however, the reorganizations taking place in the field run counter to these concepts. Changes to date have largely been done along organizational lines. To the Department's credit, streamlining efforts have been effective in reducing layers of management. The most dramatic change, as you know, was the elimination of the Regional Office function, where there is now a direct line of communication from headquarters to the field. However, most changes to date have been along organizational "cylinders". The idea for a community-first, placed-based delivery structure is still evolving.

Part of the problem is the need for an overall management of "one" Department. As it currently stands, when staffing reductions are identified, it generally becomes a pro-rata allocation among Assistant Secretaries. System development strategies are largely along organizational lines. The Deputy Secretary, CFO and Budget Officer must have a greater role in programmatic management decisions in the Department. Changes that take place should be based on what is good for HUD as a whole. Someone other than Assistant Secretaries should be making those decisions and assuring a comprehensive implementation.

To effectively managing the array of HUD programs with reduced staffing levels is a tough job. As HUD continues to downsize, there is a increased need to clarify HUD's delivery structure and outline the role of HUD staff in that structure. The number of programs HUD operates has not changed significantly over the years, yet the number of staff operating those programs has been drastically reduced. Plans on HUD's delivery structure are continuing to change. HUD needs to clarify its mission and define it more narrowly than "Creating Communities of Opportunities". Perhaps the real focus needs to be on "decent, safe and sanitary housing" for every American. HUD needs to match resource levels and capabilities with program needs. Also, HUD

needs a means to measure productivity and results.

As HUD continues to downsize, there should be no expectation that HUD staff can be all things to all people. Management must provide a clear understanding to their staff as to their role in policy development, providing technical assistance, motivating the community, overseeing program implementation and taking enforcement action for inadequate performance. With the serious reduction in staffing, we would encourage greater emphasis on implementation and enforcement.

The Government Performance and Result Act will soon require annual performance plans and performance measures throughout the Government. HUD has a number of initiatives in process to increase the use of performance measures in managing its programs and operations. During FY 95 and 96 agreement was reached with OMB as to 43 HUD performance measures. We are concerned that for 30 of those measures HUD has neither collected the data or fully defined the measure. We have recommended that the Chief Financial Officer develop a coordinate plan of action to accomplish the objectives of GPRA.

Efforts are underway to streamline and change many of the ways that HUD does business. For example, House Bill HR 2, will shift many of HUD's Public Housing roles to the States, localities and PHAs. House Bill HR 217 will consolidate federal programs for homeless assistance. The enactment of these bills would more narrowly define HUD's role as oversight and enforcement. In my opinion, even with such changes, HUD still won't have the resources to carry out their more narrowly defined roles. We believe there is a need to segregate the workload based on risk, define the strategies for different risks, establish realistic performance measures and develop a real enforcement capability.

Fiscal year 1996 is the sixth year that HUD has been subject to the audit under the CFO Act. Many of the material weaknesses and reportable conditions we are reporting on this year are the same as previous reports. HUD is making some progress in correcting reported weaknesses. For the most part, however, progress has been at a slow pace in large part because HUD needs to address issues that fundamentally impact HUD's internal control environment. HUD needs to address the following issues:

- the upgrading of financial management systems

- correcting of resource management shortcomings,
- improving performance measures for programs, and
- addressing weaknesses with its management control program.

We are working closely with HUD managers to resolve the issues I have discussed today. Many are long standing issues not easy to resolve. The problems discussed above are part of the reasons GAO designated HUD as a high risk agency. The administration and Congress must work together to implement a strategy to restructure HUD programs in line with its management capacity.